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April 6, 2005

VIA HAND DELIVERY

Pat Miller, Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37219

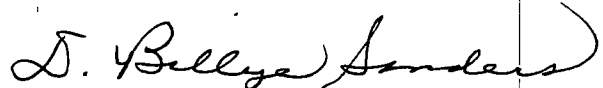
Re: Petition of Chattanooga Gas Company for Approval of
Adjustment of its Rates and Charges and Revised Tariff
Docket Number 04-00034

Reply Testimony of Michael J. Morley

Dear Chairman Miller:

Enclosed you will find the original and thirteen copies of Chattanooga Gas Company's Reply to the Affidavits of Stephen N. Brown and Daniel W. McCormac which were filed on behalf of the Consumer Advocate and Protection Division of the Office of the Attorney General.

Sincerely,



D. Billye Sanders
Attorney for Chattanooga Gas
Company

DBS/hmd

1
2
3 **BEFORE THE**
4 **TENNESSEE REGULATORY AUTHORITY**
5
6

7 **RESPONSE TESTIMONY OF MICHAEL J. MORLEY**
8 **EXHIBIT NO. RECON-2 TO**
9 **CHATTANOOGA GAS COMPANY'S**
10 **PETITION FOR RECONSIDERATION**
11

12 **IN RE:**
13 **DOCKET NO. 04-00034**
14
15

16 **Q. Please state your name, position and address.**

17 A. Michael J. Morley, Director, Financial Accounting, AGL Services Company. My
18 business address is 10 Peachtree Place, Location 1180, Atlanta, Georgia 30309.

19 **Q. Have you previously filed testimony in this proceeding?**

20 A. Yes. I previously filed direct and rebuttal testimony. I also provided testimony in
21 support of Exhibit No. Recon-2 to Chattanooga Gas Company's ("CGC" or
22 "Company") Petition for Reconsideration.

23 **Q. What is the purpose of this testimony?**

24 A. The purpose of this testimony is to respond to the supplemental testimony of Dr.
25 Stephen N. Brown and the revised exhibits of Mr. Daniel W. McCormac filed on
26 behalf of the Consumer Advocate and Protection Division ("CAPD") of the
27 Attorney General's Office of the state of Tennessee on March 30, 2005.

28
29 Dr. Brown's supplemental testimony does very little to discuss the capital
30 structure issue to which he was to respond. The TRA has already determined the
31 methodology for determining the appropriate capital structure. The CAPD did not

1 seek reconsideration of the Authority's capital structure methodology and has lost
2 the opportunity to do so. The purpose of Exhibit No. Recon-2 was to provide the
3 necessary information to determine the capital structure based on the TRA's
4 methodology. Part (1) of the motion issued February 28, 2005 by Tennessee
5 Regulatory Authority ("TRA" or "Authority") Chairman Pat Miller and adopted
6 by the TRA stated the following:

7
8 "Regarding the capital structure, I move that in order for the Authority
9 to properly consider the new evidence on capital structure introduced
10 into the record on December 31, 2004, Chattanooga Gas Company is
11 ordered to provide additional testimony or supporting documentation
12 regarding Exhibit No. Recon-2 no later than March 14, 2005. Such
13 additional material should include all assumptions used to derive the
14 projected capital structure, explanation why equity and debt ratios
15 drastically changed from December 31, 2003 to the subsequent
16 reporting periods, and other relevant documentation."

17
18 Thus, the sole issue to be addressed is AGL Resources Inc.'s ("AGLR") capital
19 structure as set forth in Exhibit No Recon-2. Accordingly, the majority of Dr.
20 Brown's supplemental testimony is outside of the scope of both Director Miller's
21 motion and the only issue to be decided in CGC's Petition for Reconsideration –
22 the actual capital structure that is consistent with the stated methodology. Instead
23 of responding to

1 these issues, Dr. Brown constructs false claims and allegations that are not only
2 irrelevant to the issue at hand but are also rash and misleading. Mr. McCormac
3 provided exhibits to reflect a lower revenue requirement and lower resulting rate
4 increase for CGC. These exhibits were based on an inappropriate and inaccurate
5 capital structure and are not within the scope prescribed by this Authority in
6 reconsidering the capital structure in this case. Again, the “alternative” capital
7 structure recommended by the CAPD is not consistent with the TRA’s
8 methodology.

9 Much like Dr. Brown’s response testimony to the Company’s direct case, his
10 supplemental testimony is designed to cast doubt on the reporting practices of
11 AGLR. Dr. Brown once again accuses AGLR of applying inconsistent capital
12 structures to its other utility subsidiaries and calls into question the integrity and
13 ethics of AGLR. Dr. Brown’s unwarranted allegations are irresponsible and
14 without basis. Dr. Brown’s continued attacks on AGLR’s integrity are
15 unprofessional and demonstrates a lack of understanding of basic ratemaking
16 principles and practices. His testimony also displays a lack of knowledge with
17 respect to the reporting requirements of AGLR as prescribed by state regulatory
18 agencies and the Securities and Exchange Commission (“SEC”).

19 **Q. How will your testimony be presented?**

20 **A.** My testimony will be presented in the following sections:

- 21 • Section I – Introduction
- 22 • Section II – Response to CAPD’s assessment of Exhibit No. Recon-2

1 December 31, 2004 capital structure. Rather, Dr. Brown has used his
2 supplemental testimony to once again present false and baseless assertions on the
3 reporting practices of AGLR and to attempt to discredit me as a witness for CGC.

4 **Q. Are Dr. Brown's assertions regarding the reporting practices of AGLR**
5 **accurate?**

6 A. No. Dr Brown either does not understand the reporting requirements and public
7 filings of AGLR, or he is simply trying to mislead the Authority to believe that
8 AGLR reports its financial information in an inconsistent and deceptive manner.
9 In our current business environment, in which the reporting of financial
10 information is under perhaps more scrutiny than ever due to accounting and
11 financial reporting improprieties and fraud by other companies, for Dr. Brown to
12 suggest in a public forum that AGLR has engaged in financial reporting
13 improprieties, without any facts or evidence, is dangerous, reckless and simply
14 not appropriate. I will address some of Dr. Brown's accusations later in Section
15 III of my testimony.

16 **Q. Why do you think Dr. Brown is attempting to discredit you as a witness?**

17 A. I believe Dr. Brown is attempting to discredit me as a witness for the same reason
18 he is trying to discredit the reporting practices of AGLR; and that is Dr. Brown
19 can find no substantive issues with the assumptions and calculations used for the
20 projected capital structures included in Exhibit No Recon-2. Therefore, since he
21 cannot disprove or discredit the information itself that is being considered, Dr.
22 Brown is simply attempting to discredit the sources of the information. The

1 insignificance of the issues themselves raised by Dr. Brown supports this view
2 and will be discussed further in section II of my testimony.

3 4 **Section II**

5 **Response to CAPD's assessment of Exhibit No. Recon-2**

6
7 **Q. What were the issues related to Exhibit No. Recon-2 that Dr. Brown**
8 **discussed in his supplemental testimony?**

9 A. Dr. Brown's issues can be summarized as follows:

- 10 • Separation of AGLR capital structure between utility and non-utility
- 11 • Exhibit No. Recon-2 does not account for known and reasonably
12 anticipated changes
- 13 • Capital Structure witness was Dr. Morin, not Mr. Morley

14 Each issue raised by Dr. Brown is baseless in nature, and he provides no evidence
15 to support his assertions. His positions are based on misinterpretation of financial
16 reports and information and an erroneous belief that most information filed with the
17 SEC is not reliable for ratemaking purposes.

18 19 **Separation of AGLR capital structure between utility and non-utility**

20 **Q. Why has the Company proposed a capital structure based on consolidated**
21 **AGLR?**

22 A. The Company proposed a capital structure based on consolidated AGLR in CGC's
23 petition for reconsideration to be consistent with the methodology used by the

1 Authority to develop its capital structure included in its order dated October 20,
2 2004. Specifically, page 44 of the Order states that “the panel found that AGLR’s
3 capital structure was the appropriate capital structure for the determination of
4 CGC’s cost of capital.”

5 **Q. Is there any relevance to Dr. Brown’s recommendation that the capital**
6 **structure of CGC should be based on AGLR’s utility subsidiaries capital**
7 **structures only?**

8 A. No. First, the Authority has already deemed that the appropriate capital structure
9 for this proceeding should be based on the capital structure of consolidated AGLR.
10 The Company, in its Petition for Reconsideration, is simply being consistent with
11 the Authority’s prescribed methodology, and, as stated, CAPD did not seek
12 reconsideration and cannot do so now.

13 Second, separation of a consolidated entity’s capital structure by individual
14 subsidiary is not practical. For AGLR, all equity is issued by AGLR and all current
15 debt issued to the public is done by AGLR’s financing subsidiaries. Therefore,
16 other than a few exceptions, no public debt resides on the books and records of
17 AGLR’s utility subsidiaries. AGLR’s capital structure is not color coded and
18 cannot be segregated by individual subsidiary.

19 Third, Dr. Brown’s recommendation to segregate AGLR’s capital structure by
20 utility and non-utility subsidiaries is contrary to the methodology he used to
21 determine the capital structure for CGC in his direct testimony.

1 **Q. How is Dr. Brown’s current recommendation contrary to his direct case?**

2 A. In his direct case, Dr. Brown proposed a capital structure based on comparable
3 companies of AGLR. The capital structures he used in his analysis did not
4 distinguish between utility and non-utility subsidiaries for AGLR or any of the
5 comparable companies he used. Dr. Brown is now apparently recommending
6 another capital structure to be considered in this case. When taking into account
7 his recommended “alternative” capital structure, Dr. Brown has recommended a
8 total of three capital structures in this proceeding.

9
10 **Known and reasonably anticipated changes**

11 **Q. Do the projected capital structures in Exhibit No. Recon-2 include all known**
12 **and reasonably anticipated changes?**

13 A. The projected capital structures in Exhibit No. Recon-2 include all known and
14 reasonably anticipated changes that would have materially impacted the capital
15 structures of AGLR. The financing of the NUI acquisition was not included since
16 it was not expected to nor did it materially impact the capital structures. This fact
17 is proven when comparing the actual and projected capital structures as of
18 December 31, 2004. The actual capital structure includes the impacts of the NUI
19 acquisition.

20 **Q. Dr. Brown states that your projected capital structure as of December 31,**
21 **2004 “missed the mark by a country mile” when compared to the actual**
22 **capital structure as of the same date. Do you agree with his statement?**

1 A. No. Dr. Brown's comparison uses the as reported December 31, 2004 capital
2 structure and does not exclude other comprehensive income ("OCI") from equity,
3 which I excluded from Exhibit No Recon-2, MJM Support – 4 and MJM Support
4 – 5, the latter two of which were provided in my testimony supporting Exhibit No
5 Recon-2. I provided an extensive explanation in that testimony as to why OCI
6 should be excluded from equity when calculating the capital structure for
7 regulatory purposes. Dr. Brown does not contest this approach in his
8 supplemental testimony, which leads me to believe that he agrees with how OCI
9 was accounted for in Exhibit No. Recon-2. My exhibit MJM Support – 4
10 provides the actual capital structure as of December 31, 2004, excluding the
11 impact of OCI, and reflects an equity ratio of 42.37%, or 2.12% lower than the
12 projected equity ratio of 44.49%. This difference equates to a variance of less than
13 5%, which I would not consider to be a "country mile " Additionally, the impact
14 on the projected average capital structure was even less. When the projected
15 average capital structure is updated for actual information as of December 31,
16 2004, the equity ratio decreases less than half a percent from 46.22% to 45.79%.
17 This is a reasonable variance between the actual and projected capital structures.

18 **Q. Dr. Brown also states that "it is not prudent to accept a forecast from a**
19 **witness who is not capable of making an accurate forecast of his own**
20 **company's capital structure just 30 days into the future." Do you agree with**
21 **this statement?**

22 A. No. Dr. Brown's "30 days into the future" statement is in reference to my
23 affidavit filed on December 3, 2004 Dr Brown believes that I only had to project

1 the capital structure as of December 31, 2004 for one month. However, the
2 purpose of my affidavit was to provide additional information regarding Exhibit
3 No. Recon-2. What Dr. Brown failed to include in his testimony was that Exhibit
4 No. Recon-2 was filed with CGC's petition for reconsideration on November 4,
5 2004, a time at which the only actual data available was through September 30,
6 2004. Therefore, the starting point for my projections had to be September 30,
7 2004 and could not have been November 30, 2004 as asserted by Dr. Brown

8 With regard to Dr. Brown's assertions around accuracy, or supposed lack thereof,
9 a forecast or projection is intended to provide estimates of future events and are
10 not intended nor expected to be *exact*. As I explained above, the projected capital
11 structure as of December 31, 2004 is quite comparable to the actual capital
12 structure. Therefore, I would consider my projected capital structure as of
13 December 31, 2004 to be accurate from the standpoint that it is within 5% of
14 actual results.

15 **Q. Dr. Brown also asserts that "Exhibit No. Recon-2 is genuinely misleading and**
16 **inaccurate" because it relies on quarterly Form 10-Qs filed with the SEC.**
17 **How do you respond to this assertion?**

18 A. I was rather surprised. Basically, under Dr. Brown's premise, the *only*
19 information filed with the SEC that can be relied upon is audited financial
20 information. Dr. Brown's assertions puzzled me for two reasons: (1) Form 10-
21 Q's are required by the SEC to provide quarterly financial information to
22 investors. They are a good thing. The public can review and analyze financial
23 information quarterly as opposed to just once a year. Most financial analysts

1 would agree that it is important to review quarterly results not only for the
2 frequency but also for the additional insight quarterly financial information can
3 provide to the operations of a company, including seasonal trends. Dr. Brown is
4 ignoring a useful and easily accessible resource for financial information by
5 dismissing Form 10-Qs as unreliable simply because they are unaudited. There
6 are severe criminal and civil penalties for individuals and companies filing false
7 information with the SEC. For AGLR, *all* filings with the SEC are done with due
8 diligence and integrity, regardless of whether or not the information is audited;
9 and (2) While Dr. Brown's belief is that the only reliable information filed with
10 the SEC is audited information, the basis for most of his arguments in his direct
11 case and supplemental testimony also is unaudited information filed with the SEC
12 and state regulatory commissions. Dr. Brown's attempt to dismiss the Company's
13 quarterly Form 10-Q's as unreliable is nothing more than a tactic to have only the
14 capital structures as of December 31 included in the determination of CGC's
15 capital structure ratemaking purposes, since December 31 historically reflects the
16 lowest equity ratio of any quarter.

17 **Q. Dr. Brown states that "10-Q data is controversial with regard to ratemaking**
18 **because the 10-Q data is not verified by an independent auditor." Do you**
19 **agree with this statement?**

20 **A** No. Regulatory agencies generally use unaudited public information more than
21 they use audited financial information. Dr. Brown is simply trying to support his
22 weak argument that only the December 31 capital structure of AGLR should be
23 considered Dr. Brown does not hesitate to use unaudited financial information in

1 an attempt to support his arguments. Following are just a few examples of Dr.
2 Brown's inconsistent treatment in using unaudited financial information:

- 3 • Dr. Brown relies on AGLR's September 30, 2004 Form 10-Q (pgs 24-25)
4 to incorrectly assert that AGLR will most likely utilize more short-term
5 debt to finance the acquisition of NUI.
- 6 • Dr. Brown relies on an application with the Virginia State Corporation
7 Commission ("VSCC") for authority for VNG to issue short-term debt and
8 long-term debt as his basis for his proposed "alternative" capital structure.
9 Dr Brown also used this same filing from 2003 in his direct testimony to
10 support his inaccurate position that AGLR arbitrarily applies capital
11 structures to its utility subsidiaries.
- 12 • Dr. Brown relies on unaudited capital structure information included in the
13 SEC's order authorizing the acquisition of NUI to wrongly claim that
14 AGLR will apply a 16.9% short-term debt ratio to NUI

15 The above information is unaudited information. I am not inferring that
16 unaudited information is not a useful source of information and cannot be relied
17 upon for regulatory purposes. Rather, I have provided the above examples to
18 confirm that Dr. Brown selectively chooses his source information and does not
19 take issue if the information is unaudited so long as it provides support to his
20 arguments. I will address each of the above examples later in my testimony.
21 Unaudited financial data can be a very useful source of information, provided the
22 user of the information understands the purpose and intent of the filing.

1 Dr. Brown also does not hesitate to use information for which the CAPD
2 previously objected, if the information can lend support to its positions

3 **Q. Please explain.**

4 A. On December 1, 2004 the TRA issued a Notice of Filing and Oral Argument,
5 which allowed any party desiring to make a filing in support of its position
6 regarding the issues raised in the Petition for Reconsideration to do so by
7 December 6. In response to that Notice, I filed an affidavit on December 6, 2004
8 to provide additional support to Exhibit No. Recon-2. On December 9, 2004, the
9 CAPD filed an objection to the submission of my affidavit into evidence, yet Dr.
10 Brown has no problem using the affidavit in an attempt to support his positions in
11 his supplemental testimony. Additionally, when CGC filed its Petition for
12 Reconsideration on November 4, 2004, a letter from Mr. Steve Lindsey to the
13 TRA was included. On November 19, 2004, the CAPD filed a letter with the
14 TRA requesting that the Directors disregard the letter from Mr. Lindsey. Dr
15 Brown, however, has included an excerpt from this letter in his supplemental
16 testimony in an attempt to support one of his positions. These are two more
17 examples of Dr. Brown selectively choosing information to support his positions.

18 **Q. You stated previously that Dr. Brown believes a single point in time,**
19 **December 31, should be used to determine AGLR's capital structure. Do you**
20 **agree with this?**

21 A. No This method contradicts basic ratemaking principles and procedures, including
22 those used by CGC and agreed to by the CAPD in this case

1 **Q. Please explain.**

2 A. CGC did not use a single point in time to determine its cost of service. CGC did not
3 use a single point in time to determine its rate base. CGC did not use a single point
4 in time to determine its cost of debt. Rather, CGC used a combination of historical
5 and forward looking twelve month periods. While it disagreed with a number of
6 items proposed by the Company, the CAPD, including Dr. Brown, never challenged
7 the use of an average projected or historical twelve month period. For example, the
8 Company did not use a point in time to determine the amount to include in rate base
9 for stored gas inventory. Rather, the Company used a rolling twelve month average
10 based on historical and forward looking information to account for the *seasonality* of
11 CGC's business. If the Company had followed Dr. Brown's approach and based its
12 stored gas inventory on audited financial information as of December 31, CGC's
13 rate base would have been substantially higher, resulting in an increased revenue
14 requirement. The Company's use of a projected average capital structure is
15 consistent with the methodology used for the other components in this case and
16 allows for the consideration of the impact seasonality has on AGLR's capital
17 structure.

18 **Q. Dr. Brown also states that using the phrase "updated to reflect actual**
19 **results" in Exhibit MJM Support – 4 is misleading. Do you agree?**

20 A. No. I do not know how providing full disclosure can be construed as misleading.
21 I included Exhibit MJM Support – 4 to provide the Authority a view of AGLR's
22 projected average capital structure with an additional quarter of actual results. In
23 my opinion, this was the appropriate thing to do – update the weighted average

1 capital structure to include the most recent data available. Dr Brown's claim is
2 just another instance in which he asserts that the only reliable and credible
3 information is audited information.

4 **Q. Dr. Brown implies that AGLR will utilize more short-term debt in the near**
5 **future based on the \$700 million bridge credit agreement signed in October**
6 **2004. Is this an accurate assessment?**

7 A. No. As stated previously, this is an example in which Dr. Brown uses unaudited
8 information in an attempt to support his position, even though he believes only
9 audited information is reliable. The \$700 million bridge credit agreement noted in
10 AGLR's September 30, 2004 Form 10-Q specifically states "the bridge facility is
11 intended only to provide us with short-term debt financing for our purchase of NUI
12 Any amount borrowed under the facility must be repaid prior to its September 30,
13 2005 expiration date." While Dr. Brown included this excerpt in his testimony, he
14 conveniently omitted the fact that AGLR issued \$332 million of equity in November
15 and \$200 million in long-term debt in December to finance the acquisition of NUI.
16 Furthermore, AGLR terminated the bridge facility in December, shortly after the
17 acquisition of NUI.

18 **Q. Will AGLR rely on short-term debt for the NUI acquisition in the same**
19 **manner it did for VNG, as Dr. Brown implies?**

20 A. No. As stated above, the acquisition of NUI has been financed through equity and
21 long-term debt. AGLR's short-term debt ratio is expected to remain consistent
22 after the acquisition of NUI.

1 **Dr. Brown's Assertion That Dr. Morin is the Capital Structure Witness, not Mr.**
2 **Morley**

3 **Q. Dr. Brown states in his testimony that you are not qualified to testify on**
4 **capital structure. Do you agree?**

5 A. No. Dr. Brown is correct that I was not the main capital structure witness for
6 CGC's direct case. However, CGC's direct case was based on a hypothetical
7 capital structure supported by Dr. Morin, not the average projected capital
8 structure of AGLR. Since the methodology prescribed by the TRA in its Order is
9 based on the projected average capital structure of AGLR, I am qualified to testify
10 in support of the Company's position on capital structure.

11 **Q. Dr. Brown states that you are "on record ...disavowing any expertise in**
12 **capital structure." Is this an accurate statement?**

13 A. No. In fact, the record will show that I did support the short-term debt ratio
14 proposed by the Company. On page 26 of his testimony, Dr. Brown did not
15 include the full answer I provided to Mr. Adams' question. Below is the question
16 from Mr. Adams and my full answer:

17
18 "Q. (Mr. Adams) Could you explain to me a little more why you chose to
19 use the 4. -- how you calculated the short-term capital 4.3 percent and the
20 ratio as opposed to using the comparable company's short-term ratio or
21 even AGA's short-term ratio?"
22

1 “A. (Mr. Morley) - Sure. We -- first of all, we calculated the short-term
2 debt ratio on Chattanooga Gas Company on a stand-alone basis to be
3 consistent with Dr. Roger Morin's capital structure as it related to long-
4 term debt and common equity. So we had to develop a short-term debt
5 ratio outside of that, and what we did was in being consistent with the
6 short-term debt ratio that we computed in our last rate case, which was in
7 Georgia for Atlanta Gas Light Company, we estimated the working capital
8 needs that Chattanooga Gas Company would need during the attrition
9 period, and I believe that's included in one of my exhibits to my direct
10 testimony.”

11 I also did not “disavow any expertise in capital structure.” I simply deferred the
12 questions regarding CGC’s proposed “hypothetical capital structure” to Dr.
13 Morin. I never stated in my written testimonies or during the hearing that I had
14 no knowledge or expertise on capital structures in general. I have extensive
15 experience in reporting and analyzing capital structures. I have also been
16 involved in a number of regulatory proceedings in which I provided input and
17 analyses on capital structures.

18 **Q. Dr. Brown also states that your capital structures are not credible. Do you**
19 **agree with this statement?**

20 A. No. As I discussed previously, projections and forecasts are intended to estimate
21 future events and, in most cases, will not equal actual results. The goal of a
22 projection or forecast is to approximate actual results within a reasonable amount.
23 Most objective accountants and financial analysts would agree that a 5% variance

1 is reasonable and would view my projected capital structures as credible. As I
2 stated in my initial testimony supporting Exhibit No. Recon-2, there are a number
3 of assumptions involved in projecting a capital structure. These assumptions
4 include forecasted net income, capital expenditures, income tax payments and
5 working capital requirements. Any variance in one or all of these assumptions
6 will result in a variance between the actual and projected capital structure.

7 **Q. Dr. Brown is very critical of your projected short-term debt balance and**
8 **ratio as of December 31, 2004 when compared to actual results. Do you agree**
9 **with his comments?**

10 A. I agree that the projected short-term debt ratio did not agree to the actual short-
11 term debt ratio for December 31, 2004. However, in developing the projected
12 capital structures for Exhibit No. Recon-2, my main focus was not on one
13 individual component of the capital structure but the entire capital structure itself.
14 Even though my projected short-term debt ratio was different from the actual
15 short-term debt ratio, my projected equity ratio was very comparable to the actual
16 equity ratio.

17 **Q. Dr. Brown appears to disagree with your statements regarding the**
18 **seasonality of AGLR's business in which December is historically its peak**
19 **short-term debt month. How do you respond to this?**

20 A. Unfortunately, his statement evidences a lack of understanding of the natural gas
21 business. If you review my Exhibit MJM Support – 5, it is clear that December is
22 the peak short-term debt month for AGLR. As I stated in my testimony filed in
23 accordance with Director Miller's order, this is the result of the seasonality of

1 AGLR's business whereby working capital use is increased during the colder
2 months of the year due to a substantial increase in natural gas volume purchases
3 coupled with increases in the price of natural gas. The sources of working capital,
4 which result from payments from customers, are not realized until the following
5 one to two months. Basically, AGLR experiences a substantial increase in
6 working capital uses during December while the corresponding sources of
7 working capital do not occur until subsequent months. This trend can be seen in
8 the historical capital structure of AGLR.

9 **Q. How do you explain short-term debt as of June 30, 2004 having the largest**
10 **balance of the five quarters presented in Exhibit No. Recon-2, including**
11 **December?**

12 A. As I stated previously, there are a number of assumptions used in projecting a
13 capital structure. When reviewing the results of a projection, the capital structure
14 should be analyzed in total, not just one component. Additionally, all periods
15 presented should be reviewed and analyzed, not just one period.

16 In my review of the projected capital structures, I did note that December was
17 lower than the historical periods (2002 and 2003) and was trending downward.
18 However, I also noted that the equity ratio was trending downward as well. More
19 importantly, I noted that the equity ratios for March and June 2005 were also
20 trending downward when compared to the equity ratios for March and June of
21 2004. Given the trends in each component of the capital structure and in all
22 periods projected, I consider the average projected capital structure in Exhibit No.
23 Recon-2 to be reasonable. Again, as stated previously, this reasonableness is

1 verified given the minor decrease in the equity ratio of the projected capital
2 structure when compared to actual results for December 31, 2004 – 46.22% to
3 45.79%.

4 5 **Section III**

6 **Response to CAPD's assertions regarding the integrity and ethics of AGLR**

7
8 **Q. Please describe the claims made by Dr. Brown regarding the reporting**
9 **practices of AGLR.**

10 **A.** Consistent with the wild accusations of his direct testimony, Dr. Brown's claims
11 are designed to cast doubt on the integrity of AGLR. His apparent goal is to
12 attempt to discredit AGLR since he has no other reasonable basis for disagreeing
13 with the projected average capital structure in Exhibit No. Recon-2. His claims
14 include the following:

- 15 • AGLR is arbitrary in its application of capital structures to its utility
16 subsidiaries.
- 17 • AGLR is ignoring Ordering Clause 18 of the Authority's Order dated
18 October 20, 2004.
- 19 • AGLR's data requires third party verification because it "does not
20 faithfully report in its SEC forms accurate descriptions of events and data
21 adverse to its interests"
- 22 • The treatment of utility subsidiaries' capital structures as confidential in
23 SEC filings is questionable.

1 **Q. Does AGLR apply arbitrary capital structures to its utility subsidiaries?**

2 A. Absolutely not. Dr Brown seems to dismiss the fact that the capital structures of
3 AGLR's utility subsidiaries are set and authorized by the applicable state
4 regulatory agencies, not AGLR itself. All of AGLR's utility subsidiaries have
5 different established regulatory capital structures. Exhibit MJM Support Response
6 – 1 provides the authorized capital structures of AGLR's utility subsidiaries. This
7 exhibit represents the capital structures AGLR applies to its applicable utility
8 subsidiaries.

9 **Q. What is the basis of Dr. Brown's claim that AGLR applies arbitrary capital**
10 **structures to its utility subsidiaries?**

11 A. Dr. Brown's claim is based on a limited review of public documents and an even
12 more limited review of the documents themselves. He reviews the selected
13 documents and then only uses information that may give credence to his
14 positions.

15 **Q. Please explain.**

16 A. With regard to VNG, Dr. Brown claims that AGLR uses a 35% equity ratio for
17 VNG based on an application with the VSCC for VNG to issue short-term and
18 long-term debt. Dr. Brown tried this argument in his direct case, which I
19 successfully rebutted in CGC's response testimony. As I testified previously in
20 my response testimony, the schedule which Dr. Brown is relying upon is a pro-
21 forma capital structure that is required by the VSCC and provides an "as if"
22 capital structure. That is, the application requires VNG to include a capital
23 structure "as if" all the debt requested for authorization were issued. Much like a

1 personal credit card credit limit, the application itself is nothing more than a
2 request for authority from the VSCC to allow VNG to issue debt and in no way
3 should be interpreted as an indication that VNG will issue debt for that amount, if
4 at all.

5 **Q. How is the application for financing authority like a personal credit card**
6 **credit limit?**

7 A. The application, once approved, gives VNG the authority to borrow up to a
8 certain amount. Most personal credit cards work the same way. The credit card
9 company provides you a “credit limit”, and you have the authority to use the card
10 up to that limit. However, just because you have the authority to borrow up to, for
11 example, \$10,000, does not mean that you will actually utilize the card up to the
12 \$10,000 limit. Yet, as I stated the VSCC requires the application to include a pro-
13 forma “as if” capital structure that includes the full requested amount.

14 **Q. Dr. Brown refers to the pro-forma capital structure of VNG as the “in-**
15 **practice” capital structure. Is this an accurate statement?**

16 A. No. Dr. Brown is attempting to mislead the Authority to consider his
17 “alternative” capital structure with his use of the term “in-practice.” This term is
18 not used in the application nor is it an accurate depiction of VNG’s actual or
19 regulatory capital structure. VNG’s equity for regulatory purposes is 54.94%, not
20 35.5% as asserted by Dr. Brown. The complete regulatory capital structure of
21 VNG is included in Exhibit MJM Support Response – 1 and in no way resembles
22 the “alternative” capital structure recommended by Dr. Brown.

1 **Q. Dr. Brown also states that AGLR is applying arbitrary capital structures to**
2 **NUI. Is this correct?**

3 A. No. As with VNG, Dr. Brown has taken a public document out of context. He
4 then molds and presents the information in a manner that best supports his
5 reckless position, regardless of fact or principle

6 **Q. What information is Dr. Brown misinterpreting?**

7 A. He is using information from the SEC's order authorizing AGLR's acquisition of
8 NUI. Included in the order is the capital structure for NUI Utilities as of June 30,
9 2004, which has a short-term debt ratio of 16.9%. Assuming and claiming that
10 the short-term debt ratio of NUI Utilities almost six months prior to the
11 acquisition is the applied or regulatory capital structure of NUI Utilities is simply
12 preposterous. First, AGLR did not even own NUI Utilities at June 30, 2004.
13 Second, the capital structures that will be applied to NUI Utilities by AGLR are
14 the authorized regulatory capital structures included in MJM Support Response –
15 1. Third, NUI Utilities consists of three separate regulated entities.
16 Dr. Brown also misrepresents a commitment by AGLR and a requirement by the
17 Public Utilities Holding Company Act of 1935 to maintain an equity ratio no less
18 than 30% for NUI. The key phrase here is *no less*. Dr. Brown is misrepresenting
19 to the Authority this commitment and requirement to mean that the equity ratio of
20 NUI Utilities will approximate 30%. This is simply not true. The capital
21 structure of NUI Utilities will be the capital structures as authorized by the
22 applicable state regulatory agencies as provided in MJM Support Response – 1.

1 **Q. Dr. Brown uses the capital structures included in VNG's financing**
2 **application and the SEC order authorizing AGLR's acquisition of NUI to**
3 **compare to your projected capital structures. Is this a valid comparison?**

4 A No. My capital structures are based on AGLR. They are not based on a VNG
5 pro-forma capital structure or an NUI capital structure as of June 30, 2004, nor
6 should they be. If Dr. Brown is really interested in comparing the capital
7 structure used by CGC to determine rates to the other AGLR utility affiliates, he
8 would use the authorized regulatory capital structures for his comparison, not a
9 pro-forma or stale capital structure.

10 **Q. Is AGLR in compliance with ordering clause 18 of the Authority's Order**
11 **dated October 20, 2004?**

12 A. Yes. Despite Dr. Brown's claim that the Company is not, CGC notified the
13 Authority on November 24, 2004 that the SEC authorized the acquisition of NUI.
14 Attached Exhibit MJM Support Response – 2 is an e-mail and press release
15 attachment that was sent to each Director. In fact, Mr. Dan McCormac of the
16 CAPD was copied on the e-mail as well.

17 **Q. Dr. Brown implies that the Company was required to provide the terms of**
18 **the NUI acquisition to the Authority. Is this correct?**

19 A. No. Ordering clause 18 is specific to "future actions taken by the SEC". CGC
20 notified the Authority of an action taken by the SEC, and that action was to
21 authorize AGLR's acquisition of NUI.

22 **Q. Does AGLR faithfully report to the SEC accurate descriptions of events and**
23 **data, regardless of the nature and impact?**

1 A. Yes. Again, Dr. Brown's accusations are completely unfounded, reckless and
2 irresponsible. AGLR applies the same reporting procedures, due diligence and
3 review process in all of its filings, regardless of the information filed.

4 **Q. Did AGLR inform the investment community that the Authority ordered a**
5 **revenue increase of \$1.3 million, as Dr. Brown asserts?**

6 A. No. However, AGLR did inform the investment community that the Authority
7 had ordered a \$1.3 million rate increase. A revenue increase is not the same thing
8 as a rate increase. The \$1.3 million rate increase includes the impact of the
9 Authority's decision to allow bad debt recovery through CGC's purchased gas
10 adjustment ("PGA"). AGLR is not assuming an additional rate increase as a
11 result of CGC's petition for reconsideration, although the Company believes one
12 is warranted. AGLR was simply providing full disclosure of the regulatory
13 decisions in Tennessee in 2004, which include a revenue increase of \$642,777
14 through base rates and bad debt recovery through CGC's PGA of approximately
15 \$640,000.

16 **Q. Dr. Brown also claims that AGLR misrepresented the ordered rate increase**
17 **in its 10-K filed February 15, 2005. Is this correct?**

18 A. No. It is rather common for companies to round numbers up or down and to use
19 the term "approximately" when reporting financial information. In this instance,
20 AGLR simply rounded \$642,777 to \$1 million and reported the information as
21 "approximately \$1 million."

22 **Q. Did AGLR discuss the bad debt recovery through CGC's PGA in the 10-K?**

1 A. AGLR did include a discussion of CGC's bad recovery through its PGA in the 10-
2 K. Dr. Brown failed to include this portion of the 10-K in his testimony. Both
3 items were separated in the 10-K to provide full disclosure of each item to
4 investors and readers of the 10-K. Additionally, while both items result in a rate
5 increase through separate mechanisms, each item's impact is different on the
6 income statement of CGC. The base rate increase results in a corresponding
7 increase to revenues, and the bad debt recovery through CGC's PGA results in a
8 reduction to operations and maintenance expense.

9 **Q. Why does AGR file its utility subsidiaries' capital structures with the SEC as**
10 **confidential?**

11 A. Contrary to Dr. Brown's claim that "it is not clear why AGLR's subsidiaries'
12 capital structures would need to be confidential", AGLR clearly states in its
13 request for confidential treatment why this information should be confidential.
14 Following is the explanation included in the confidential treatment request filed
15 with the SEC:

16 "AGL Resources requests that the Commission afford confidential
17 treatment to Exhibits 1,4,5,6, and 7 because they contain confidential
18 business information within the exemption provided by 5 U.S.C.
19 §552(b)(4) The information in these Exhibits reveals proprietary
20 financial data that may cause competitive harm to AGL Resources if
21 released to competitors or to the public. This information is not disclosed
22 in AGL Resources' other public filings These Exhibits contain
23 information that AGL Resources would not customarily release to the

1 public. For these reasons, public disclosure of the information in these
2 Exhibits is not necessary or appropriate in the public interest or for the
3 protection of investors or consumers.”

4 The above statement by AGLR clearly explains why it requests confidential
5 treatment of its utility subsidiaries in its 35-CERT filing with the SEC. This is yet
6 another example of Dr. Brown failing to include all relevant information in his
7 testimony. He consistently selects certain excerpts in an attempt to support his
8 position and excludes those that clearly contradict his position.

9 **Q. Did the CAPD request the confidential schedules referred to by Dr. Brown?**

10 A. Yes. The CAPD made an informal data request to the Company on March 17,
11 2005.

12 **Q. Did the Company provide the requested information?**

13 A. Yes. The Company provided the requested information under the protective order
14 issued in this docket on March 28, 2005.

16 **Section IV**

17 **Summary and Conclusions**

18
19 **Q. Please summarize your response to the CAPD’s supplemental testimony.**

20 A. As I previously stated, the TRA has already determined the methodology for
21 determining the appropriate capital structure, and the CAPD did not seek
22 reconsideration of the Authority’s capital structure methodology. The purpose of
23 Exhibit No Recon-2 was to provide the necessary information to determine the

1 capital structure based on the TRA's methodology, and Director Miller's Order
2 set forth a procedure to provide additional information in support of Exhibit No
3 Recon-2. The supplemental testimony of Dr. Brown is nothing more than a
4 continuation from his direct case in which he recklessly attacks the integrity and
5 ethics of AGLR. Dr. Brown also attacks my qualifications as a witness on capital
6 structure. However, Dr. Brown's positions lack merit and are not based on fact.
7 He attempts to support his positions with misleading information and conspiracy
8 theories. Dr. Brown either does not fully understand the subject matter of his
9 testimony, or he is attempting to mislead the Authority.

10
11 CGC has provided all information necessary for a reasonable person to analyze
12 and assess the reasonableness of the projected average capital structure provided
13 by CGC in Exhibit No. Recon-2. This information included detail support,
14 assumptions and the analytical process used in calculating the projected average
15 capital structure. Based on Dr. Brown's supplemental testimony, in which he
16 focused on issues and subjects irrelevant to this matter, I can only conclude that
17 he substantially agrees with the methods and procedures used in calculating the
18 projected average capital structure.

19
20 Dr. Brown's objective is to convince the authority to use AGLR's capital
21 structure as of December 31, a point in time in which AGLR's short-term debt
22 ratio is at its highest and equity ratio is at its lowest. Therefore, he has resorted to
23 a strategy of attack and discredit, regardless of the lack of evidence, in an effort to

1 dismiss all information other than audited information, which, coincidentally, is
2 only information as of December 31. Acceptance of Dr. Brown's "one point in
3 time" approach would understate the equity ratio of AGLR and is in complete
4 contrast to basic ratemaking principles and methodologies, including the use of
5 known and reasonably anticipated changes and estimates. This approach is not
6 even consistent with the methodologies used in both CGC's and the CAPD's
7 direct cases. The capital structure of AGLR should be based on an average
8 capital structure, which is consistent with methodologies used in this case and
9 accounts for the seasonality of AGLR's business.

10
11 The exhibits provided by Mr. McCormac are based on information that is not only
12 irrelevant to this issue but is also inaccurate and in no way reflect the capital
13 structure of AGLR or its utility subsidiaries. Therefore, these exhibits do not
14 merit consideration in this proceeding.

15 **Q. Does this conclude your testimony?**

16 **A** Yes.

**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

IN RE:)

PETITION OF CHATTANOOGA GAS)
COMPANY, FOR APPROVAL OF)
ADJUSTMENT OF ITS RATES AND)
CHARGES AND REVISED TARIFF)

DOCKET NO. 04-00034

VERIFICATION

STATE OF GEORGIA)
COUNTY OF FULTON)

I, Michael J. Morley, being first duly sworn, state that I am the Director of Financial Accounting for AGL Services Company and that I am authorized to testify on behalf of Chattanooga Gas Company in the above referenced docket and that the foregoing pre-filed testimony and the Exhibits attached thereto are true and correct to the best of my knowledge, information and belief.



Michael J. Morley

Sworn and subscribed before me this 5th day of April, 2005.



Notary Public

My Commission Expires: Notary Public - Fulton County, Georgia
My Commission Expires June 30, 2006

Chattanooga Gas Company
Docket No. 04-00034
Exhibit MJM Support Response - 1
Authorized Capital Structures of AGLR utility Subsidiaries

(Based on Most Recent Rate Decisions)

	AGLC	CGC	VNG
	% Total Capitalization	% Total Capitalization	% Total Capitalization
ST Debt	2.25%	16.40%	9.45%
LT Debt	50.75%	37.90%	35.05%
ITC	0.00%	0.00%	0.56%
Preferred Stock	0.00%	10.20%	0.00%
Common Equity	47.00%	35.50%	54.94%
Return on Investment			
Docket/Case No.	14311-U	04-00034	PUE-96-0227

	City Gas of Florida	Elkton	Elizabethtown
	% Total Capitalization	% Total Capitalization	% Total Capitalization
ST Debt	7.72%		
LT Debt	40.32%	52.16%	47.01%
ITC			
Preferred Stock			
Customer Deposits	4.86%		
(1) Def Taxes-Zero Cost	9.88%		
(1) Tax Credit-Zero Cost	0.45%		
Common Equity	36.77%	47.84%	52.99%
Return on Investment			
Docket/Case No.	030569-GU	8449	GR02040245

- (1) City Gas of Florida excludes deferred taxes as a rate base deduction but includes them in its capital structure

From: Archie Hickerson
Sent: Monday, November 29, 2004 9:07 AM
To: 'Pat.Miller1@state.tn.us'; 'Debi.Tate@state.tn.us'; 'Sara.Kyle@state.tn.us';
'Ron.Jones@state.tn.us'
Cc: dbs@wallerlaw.com; 'Dan.McCormac@state.tn.us'; 'Richard.Collier@state.tn.us'
Subject: AGL SEC Approval Release 11 24 04

Chairman Miller
Directors Tate
Director Kyle
Director Jones

In order to keep the Authority informed of the progress of AGL Resources' acquisition of NUI, I am forwarding a copy of the November 24, 2004 news release announcing the SEC approval of the acquisition and management appointments.

If you have any questions, please give me a call at 404 584 3855.

AGL Resources
Atlanta Gas Light
Chattanooga Gas
Virginia Natural Gas
AGL Networks
Sequent Energy Management

404 584 4000 phone
www.aglresources.com

Ten Peachtree Place
Atlanta, GA 30309

Chattanooga Gas Company
Docket No 04-00034
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News Release

For Immediate Release

date Nov. 24, 2004

contact **Financial**
Steve Cave
404 584 3801 (office)
678 642 4258 (cell)
scave@aglresources.com

Media
Nick Gold
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SEC Approves AGL Resources' Acquisition of NUI Corp. AGL RESOURCES TO BE EAST COAST'S LARGEST NATURAL GAS DISTRIBUTOR *MANAGEMENT APPOINTMENTS ANNOUNCED*

ATLANTA, Ga — Nov. 24, 2004 — The Securities and Exchange Commission (SEC) today approved the acquisition by AGL Resources Inc (NYSE:ATG) of NUI Corp. (NYSE:NUI), a diversified energy company with natural gas utilities, storage and pipeline operations, for \$13.70 per share in cash and the assumption of NUI's debt at closing. The transaction is expected to close Nov. 30, 2004.

The addition of NUI will expand AGL Resources' base of urban utility operations to 2.2 million customers in six states and strengthens its position as the largest operator of natural gas utility assets in the eastern United States. In 2003, AGL Resources was named Gas Company of the Year by Platts Global Energy.

"AGL Resources and NUI had requested expedited approval to close the transaction prior to year end — before the peak of the winter so that NUI customers would continue to receive natural gas service without interruption," said Paula Rosput Reynolds, chairman, president and chief executive officer of AGL Resources. "We are gratified that regulators in three states and the federal government agreed with this priority and approved this acquisition in an expedited time frame."



Reynolds said that beginning in the new year, the company would announce commitments to all of its gas customers as to the types and time frame in which they can expect to experience service improvements.

AGL Resources announced its plans to acquire the financially troubled NUI in July of this year. The New Jersey Board of Public Utilities (NJBP) unanimously approved the regulatory settlement agreement (related to Elizabethtown Gas) on Nov. 9, 2004. The terms of the agreement included.

- An accelerated payment of the \$21 million in customer refunds outstanding from the \$28 million in refunds ordered by the NJBP. This averages approximately \$75 per residential customer beginning with the January billing cycle
- A base rate freeze for a five-year period, with customers participating in any over-earnings in the fourth and fifth years
- A retirement enhancement for New Jersey-based employees
- A three-year asset-management agreement between Elizabethtown Gas and Sequent Energy Management, a wholly owned subsidiary of AGL Resources

AGL Resources also announced the reorganization of its six-state territory into two divisions:

- Mid-Atlantic Operations — Maryland, New Jersey and Virginia
- Southern Operations — Florida, Georgia and Tennessee

The divisions will be overseen by Hank Linginfelter, who will become senior vice president, Mid-Atlantic Operations, and Suzanne Sitherwood, who was named senior vice president, Southern Operations.

Linginfelter, who is based in Norfolk, Va., will continue to serve as president of Virginia Natural Gas and will add responsibilities for the NUI distribution operations, which include Elizabethtown Gas (New Jersey), Elkton Gas (Maryland) and Virginia Gas (Saltville, Va.).

Sitherwood, who is based in Atlanta, formerly served as vice president, gas operations and capacity planning. Sitherwood will succeed Isaac Blythers as president of Atlanta Gas Light and Chattanooga Gas and will also be in charge of NUI's City Gas of Florida. Blythers, who has served as president of Atlanta Gas Light and Chattanooga Gas since 2002, will join the office of the CEO until his retirement on May 1, 2005, after 30 years of service.

AGL Resources
Atlanta Gas Light
Chattanooga Gas
Virginia Natural Gas
AGL Networks
Sequent Energy Management

404 584 4000 phone
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Atlanta, GA 30309

Chattanooga Gas Company
Docket No. 04-00034
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Eric Martinez, formerly senior vice president at AGL Resources division, Pivotal Energy Development, will report to Linginfelter and will become vice president and general manager of Elizabethtown Gas. Charles Rawson, formerly managing director, wholesale services, at Atlanta Gas Light, will report to Sitherwood as vice president and general manager, City Gas of Florida.

Three Atlanta Gas Light region managers will assume duties in the NUI franchise areas as AGL Resources seeks to unify and improve operational efficiencies across the company. Eddie V. Wood and Don Carter will assume responsibilities at Elizabethtown Gas, while Eduardo Noriega will take on duties at City Gas of Florida.

Beth Reese will become vice president, customer service, and Scott Carter is newly appointed as vice president, regulatory affairs. Jodi Gidley succeeds Sitherwood as vice president of gas operations and capacity planning. Patricia Keefe, who was vice president at Elizabethtown Gas, will join the AGL Resources regulatory affairs organization.

Other recent appointments at AGL Resources include Melanie Platt, who became senior vice president of human resources and chairman of the AGL Resources Foundation. In addition, Ralph Cleveland will serve as senior vice president, engineering and operations while Bryan Batson will become senior vice president, regulatory affairs and customer service.

Myra Coleman has been named executive director of corporate governance and securities counsel. John Ebert was named executive vice president of Pivotal Energy Development, and Dat T. Tran will become chief counsel for regulatory affairs.

NUI's shareholders overwhelmingly approved the AGL Resources acquisition on Oct. 21, 2004. On Nov. 15, AGL Resources made a public offering of 11,044,000 shares of its common stock. The net proceeds from the offering of approximately \$332 million will be used to purchase the outstanding capital stock of NUI and to fund AGL Resources' recently completed purchase of Louisiana-based Jefferson Island Storage & Hub LLC. The remaining net proceeds will be used to repay short-term debt and for general corporate purposes.

About AGL Resources

AGL Resources (NYSE: ATG) is an Atlanta-based energy services holding company and was named 2003 Gas Company of the Year by Platts Global Energy Awards. Its utility subsidiaries - Atlanta Gas Light, Virginia Natural Gas and Chattanooga Gas - serve approximately 1.8 million customers in three states. Houston-based subsidiary Sequent Energy Management provides natural gas asset management, producer, storage and hub services. As a member of the SouthStar